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IN THE

Supreme Court of the United States

OCTOBER TERM, 1935.

JOHN A. NELSON COMPANY, PETITIONER,

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE.

ON A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

BRIEF FOR PETITIONER.

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THE COURT PRESS, N. Y. C.

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OPINIONS BELOW.

The opinion of a division of the Board of Tax Appeals (R. 26-39) is reported in 24 B. T. A. 1031. This opinion was reviewed by the full Board (R. 39) and another opinion (R. 45-61) reported in 28 B. T. A. 529. The opinion of the Circuit Court of Appeals (R. 74-78) is reported in 75 Fed. (2d) 696.

JURISDICTION.

Judgment of the Circuit Court of Appeals was entered on February 23, 1935 (R. 78). The petition for certiorari was filed May 20, 1935, and granted October 14, 1935. The jurisdiction of this Court rests on Section 240(a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED.

Petitioner, a corporation, transferred substantially all of its assets to another corporation in ex-

change for all of the latter's preferred stock and a cash sum. Petitioner immediately distributed the preferred stock and cash so received to its own stockholders. Petitioner, though inactive, did not dissolve. The question is whether this constitutes a reorganization within the meaning of Section 203(h) of the Revenue Act of 1926, the portion of which here material, is as follows:

> "(1) The term 'reorganization' means (A) a merger or consolidation (including the acquisition by one corporation of * * * substantially all the properties of another corporation) * * *."

If, as petitioner contends, the answer is in the affirmative, no taxable gain or deductible loss results; if in the negative, as respondent contends, gain or loss does enter.

STATUTES INVOLVED.

The statutes involved are set forth in the Appendix, *infra*, pp. 23-25. Unless otherwise indicated, all section references in this brief will apply to the Revenue Act of 1926.

STATEMENT OF CASE.

The issue here presented is not the creature of the parties, but of the Board of Tax Appeals (R. 39-40). The parties stipulated that there was a reorganization and their only contest was as to the tax effect of the reorganization (R. 13). A division of the Board promulgated an opinion (24 B. T. A. 1031) deciding the effect of the agreed reorganization (R. 26-39, especially 37-39). Thereafter, the Board, on its own motion, withdrew the opinion and ultimately promulgated another opinion (five members concur-

ring in the result only, and one dissenting) declaring that there was no reorganization (R. 45-61, especially 58-60). The Circuit Court of Appeals affirmed the Board (R. 78).

Petitioner was in the adding machine business (R. 12). On November 18, 1926, it entered into an agreement with Elliott-Fisher Company with respect to that business (R. 13). The agreement provided, among other things, for the organization by Elliott-Fisher Company of a new company with a capitalization of 12,500 shares of preferred stock and 30,000 shares of common stock (R. 14, 16). The terms of these stocks were set forth in detail (R. 14-16). The preferred stock was to carry a 7% cumulative dividend and have no voting power except on certain dividend arrearages (R. 14-15). The new company was to have the right, on advance notice to stockholders, to retire the stock at designated prices on dividend dates (R. 14-15). Petitioner agreed to transfer all of its assets (except cash of $100,000, which constituted less than 3% of its assets), subject to all its liabilities (except for certain bonuses to employees, and for 1926 federal income taxes), in exchange for the 12,500 shares of preferred stock and $2,000,000 in cash to be raised by the sale for that amount by the new company of 30,000 shares of common stock to Elliott-Fisher Company (R. 17, 18, 21-22). The new company was to have the right to use petitioner's name (then called the Sundstrand Corporation) and petitioner agreed, upon request, to change its own name for the purpose (R. 19). The date for the consummation of the transfer was fixed at December 31, 1926 (R. 20).

On November 18, 1926, a special meeting of petitioner's stockholders was held at which the foregoing agreement, described in the minutes as "providing

for a reorganization" of the company and sale and transfer of its assets, was approved; and it was voted that upon the consummation of the transfer, the preferred stock and cash to be received from the new company be immediately distributed to petitioner's stockholders in the order of their preferential right (R. 23-24). It was also voted that "after the distribution of the proceeds in accordance with the reorganization plan", petitioner be dissolved (R. 24). It was voted, too, that in the meantime petitioner's name be changed to John A. Nelson Company so as to enable it to comply with the agreement (R. 24).

On December 31, 1926, the transfer and distribution were consummated, pursuant to the agreement of November 18, 1926 and the vote of petitioner's stockholders at the meeting of November 18, 1926 (R. 13).

SPECIFICATION OF ERRORS TO BE URGED.

The Circuit Court of Appeals erred:

1. In failing to hold that the exchange of substantially all the assets of a corporation for all the preferred stock of the acquiring corporation and a cash sum, followed by the distribution of the preferred stock and cash by the first company to its stockholders, is a reorganization within the definition of that term as set forth in Section 203(h) (1) of the Revenue Act of 1926.

2. In holding that said transaction constitutes a sale and not a reorganization.

3. In holding that the dissolution of the corporation transferring the assets, and/or the acquisition by the transferring corporation of a controlling interest in the affairs of the transferee is a prerequisite to the existence of a reorganization.

4. In affirming the decision of the Board of Tax Appeals.

SUMMARY OF ARGUMENT.

The statute says, in so many words, that a reorganization takes place through a merger or consolidation, including the acquisition by one corporation of substantially all the assets of another. This does not mean that the mere acquisition of a corporation's assets, without more, is a reorganization; but it does mean that such an acquisition, coupled with a continuing interest in the affairs of the transferee by the transferor, constitutes a reorganization. *Pinellas Ice and Cold Storage Company* v. *Commissioner*, 287 U. S. 462.

The required continuing interest is best reflected by stock. *Keen & Woolf Oil Company* v. *Commissioner*, 49 Fed. (2d) 45 (C. C. A. 5). Preferred stock is a proprietary interest in the affairs of a corporation. Limitation as to dividends, lack of voting power, redeemability, in no way impair the status of preferred stock as a proprietary interest in the affairs of a corporation. *Atlantic City Electric Co.* v. *Commissioner*, 288 U. S. 152. Therefore, the transfer of substantially all of a corporation's assets in exchange for all of the preferred stock of the transferee corporation—which was the transaction in the case at bar—constitutes a reorganization. (Cash was also involved, but by virtue of Section 203(e), it has no bearing on the basic question.)

The lower court went on the view that to spell reorganization, it must also appear, in addition to the foregoing, that the transferor acquires or remains in control of the affairs of the transferee, and/or that

the transferor dissolves. *West Texas Refining and Development Company* v. *Commissioner*, 68 Fed. (2d) 77 (C. C. A. 10); also, *The G. and K. Manufacturing Company* v. *Commissioner*, 76 Fed. (2d) 454 (C. C. A. 4), certiorari granted October 14, 1935. (The opinion in the latter case questioned whether substantially all of the assets were transferred and the decision seems to rest on that phase.) Not only is there no statutory sanction for such superimposed requisites, but the legislative history of the various revenue acts since 1918 also establishes that Congress did not intend that there should be such requisites. Furthermore, the years of administrative construction under the various acts, followed by re-enactment of the statute without change in respects here material, make clear that the Department charged with the execution of the statute never construed a reorganization to entail such requisites, and that Congress repeatedly stamped such construction with approval. *Minnesota Tea Company* v. *Commissioner*, 76 Fed. (2d) 797 (C. C. A. 8); *John J. Watts* v. *Commissioner*, 75 Fed. (2d) 981 (C. C. A. 2); *Zellerbach Paper Co.* v. *Helvering*, 293 U. S. 172, 178.

ARGUMENT.

A synoptic preliminary statement may be of help in positing the issue in its precise setting. Section 203(a) of the Revenue Act of 1926 brings the gain or loss on every sale or exchange of property into the tax calculation unless embraced by certain specific exceptions. One of the exceptions so specified has to do with certain types of reorganization, and the question presented to this Court for determination is whether the exception rather than the general rule applies to the environal facts here involved.

Assuming the exception does apply—and here is

the phase that is noteworthy *in limine*—there is no *exemption* from income tax; there is merely *deferment*. The *status quo* continues, pending a sale or exchange to which the general rule rather than the exception applies. Furthermore, even the deferment cuts two ways. It not only postpones gain, but also denies loss. The rule of strict construction applicable to exceptions and exemptions does not, therefore, invade this field. Any contraction of the scope of the exception here under consideration would, to be sure, narrow the band of transactions where gain can be deferred, but by the same token, it would widen the field of losses that could be immediately deducted. Under such circumstances, the interpretative approach should be neither with strictness nor bounty, but rather precision.

There is another phase that may, perhaps, best be disposed of in this prelude. The generic principle of non-recognition of gain or loss in a reorganization applies where the consideration taken back is stock or securities (Section 203(b) (2) (3)). However, under Section 203(e), cash or other property may accompany the stock or securities and still hold inviolable the non-recognition rule, if the cash or other property is distributed by the receiving corporation pursuant to the reorganization plan. In the case at bar, the consideration received by petitioner was preferred stock and cash, but as immediate distribution of the cash (and the preferred stock) was planned and consummated, the fact that cash was in part involved is rendered inconsequential and forms no part of the *desiderata*.

We are now, perhaps, somewhat better equipped to consider the question at issue in this case in the form to which it thus reduces itself, namely, whether an exchange by a corporation of substantially all of

its assets for all of the preferred stock of the acquiring corporation, constitutes a reorganization resulting in no taxable gain or deductible loss.

I.

The exchange of substantially all of the assets of a corporation for a stock interest in the transferee corporation squarely meets the statutory requirements for reorganization under Section 203(h) (1) (A).

In determining whether a transaction constitutes a reorganization in contemplation of the Revenue Act of 1926, we are not left to dabble with imponderables or generalities. The statute describes by metes and bounds, the niche into which the transaction must fit, to yield an affirmative answer. The part that counts is Section 203(h):

> "(1) The term 'reorganization' means (A) a merger or consolidation (including the acquisition by one corporation of * * * substantially all the properties of another corporation) * * *."

At first blush, it would appear that through the parenthetical material, the statute covers the case at bar *"ipsissimis verbis"*. However, the relationship of the parenthetically enclosed words to those of "merger or consolidation" immediately preceding, became a matter for judicial inquiry. The Board of Tax Appeals and some of the courts veered towards a narrow construction, which in effect blighted the scope of the parenthetical clause almost to extinction, and made as the *sina qua non,* a technical merger or consolidation. On the other hand, it was the view of other judicial bodies that the part in parentheses may

be considered wholly apart from and without reference to the words preceding and outside the parentheses.

It was inevitable that this Court be called upon to calm the turbulent waters, and it did so in *Pinellas Ice & Cold Storage Co.* v. *Commissioner*, 287 U. S. 462, as follows:

> "The words within the parenthesis may not be disregarded. They expand the meaning of 'merger' or 'consolidation' so as to include some things which partake of the nature of a merger or consolidation but are beyond the ordinary and commonly accepted meaning of those words—so as to embrace circumstances difficult to delimit but which in strictness cannot be designated as either merger or consolidation."

In other words, the court declared that while the predicate of the statutory definition of a reorganization in part (A) was that of merger and consolidation, the words in parentheses were added by Congress to get away from the narrow, limited, and technical meaning of "merger" and "consolidation". Affirmatively what was done through the parenthetical material was to expand and enlarge on the accepted meaning of the basic words.

The precise scope of the enlargement was likewise pointed out by the Court. Before quoting it, a word about the facts in the *Pinellas* case will supply a needed background. What was involved there, was a sale of assets for cash and a promissory note payable in three to four months. That of course, had not even the faintest semblance or slightest practical assimilation to a merger or consolidation, no matter

how expansive a view of those words is applied. Nevertheless, the taxpayer contended that the sale was a reorganization. The Court replied:

> "But the mere purchase for money of the assets of one company by another, is beyond the evident purpose of the provision, and has no real semblance to a merger or consolidation. Certainly, we think that to be within the exemption the seller must acquire *an interest* in the affairs of the purchasing company more definite than that incident to ownership of its short term purchase money notes. This general view is adopted and well sustained in *Cortland Specialty Co.* v. *Commissioner of Internal Revenue*, 60 F. (2d) 937, 939, 940. It harmonizes with the underlying purpose of the provisions in respect of exemptions and gives some effect to all the words employed."

In the *Cortland Specialty Co.* case cited with approval in the foregoing quotation, the taxpayer made the same contention as before the Supreme Court. The Second Circuit held that "a sale of the assets of one corporation to another for cash without the retention of *any interest* by the seller in the purchaser is quite outside the objects of merger and consolidation statutes". Certiorari was denied, 288 U. S. 599.

Thus it will be seen that the exterior boundaries of the merger or consolidation concept as modified and expanded by the parenthetical words, are the continuation by the seller of "an interest in the affairs of the purchasing company". Note that the extent of the interest is neither described nor made material. "Any interest" were the conditioning words in the *Cortland Specialty Co.* opinion. Quality not quantity controls. It is only in part (B) of Section

203 (h) that quantity assumes importance. We mention this, because as shall be seen later, the Court below confounded parts (A) and (B) in this respect. All that is required for (A) is that there be *a* continuity of an interest.

What constitutes "an interest" is a question that need not long arrest attention—at least not for the purposes of this case. Section 204 (a) (7) of the Act, which is interlinked with Section 203, says that if in a reorganization, an "interest or control" of 80% or more in the assets involved, remains in the same persons, then; the acquiring corporation stands in the shoes of the transferor for the purpose of admeasuring gain or loss on a subsequent sale. What was meant by "interest" came up for adjudication in *Keen & Woolf Oil Company* v. *Commissioner,* 49 Fed. (2d) 45 (C. C. A. 5). The court said:

> "'Interest' refers to ownership, and may be retained either through preferred or common stock, and independently of voting power."

This view is likewise proclaimed in the *Cortland Specialty Co.* case, when the court said:

> "As no stock was issued against the transfer, the conditions for an exemption were not fulfilled * * *."

The same point also came up in *Mead Coal Co.* v. *Commissioner,* 72 Fed. (2d) 22 (C. C. A. 4), and the court declared:

> "It should not be necessary to add that the issuance to the old stockholders of stock in the new company provided the essential element, as the term reorganization has been defined, of a continuity of interest from the old corporation to the new."

It is thus authoritatively established that the exchange of substantially all the assets of a corporation for a stock interest in the transferee corporation squarely meets the statutorily defined concept of reorganization in Section 203(h) (1) (A) of the Revenue Act of 1926. That the preferred stock received by petitioner qualifies as a stock interest and a proprietary interest in the affairs of the transferee, will be the thesis of the next point in the argument.

II.

Preferred stock, though limited as to dividends and voting privileges, and subject to retirement, is a proprietary interest in the affairs of a corporation.

It would be a work of supererogation to linger here too long in the light of this Court's holding in *Atlantic City Electric Company* v. *Commissioner,* 288 U. S. 152. The taxpayer there contended that in determining whether (for the purposes of consolidated returns) two corporations really represent a single enterprise, no common ownership need exist as to preferred stock with voting rights, where the stock is redeemable at any time and has a limited interest in dividends. In rejecting the contention, this Court, through Mr. Chief Justice Hughes, said:

> "Despite redeemability and the limitation of dividends, the owners of the preferred stock were not in the position of creditors, but were stockholders with a proprietary interest in the corporate undertaking * * *."

Lesser luminaries in the field include the *Keen & Woolf Oil Co.* case, *supra,* characterizing preferred stock as representing an ownership interest, regardless of voting power. So, also, *I. Unterberg & Co.* v. *United States,* 64 Ct. Cls. 197, where the taxpayer unsuccessfully contended that (for invested capital

purposes) certain notes were the equivalent of preferred stock, the Court saying:

> "Preferred stock entitles the holder to an interest in the assets of the corporation, with a voice in its management, and to the right to share in its surplus profits."

Even though redemption is at the option of the stockholders, preferred stock makes for a proprietary and not a creditor relationship, *Finance & Investment Corp.* v. *Burnet,* 57 Fed. (2d) 44 (C. A. D. C.):

The cases are too multitudinous to permit selective citation where taxpayers contended for deductibility of dividends on retirable preferred stock as being the equivalent of interest, only to be consistently and properly turned down by the courts and the Board of Tax Appeals. *National Cottonseed Products Corp.,* 28 B. T. A. 67, is indeed interesting in this respect, involving as it did preferred stock where the issuer concurrently entered into an agreement to repurchase the stock at fixed dates.

As applied to the very issue at bar, the Board of Tax Appeals held an exchange of assets for preferred stock and cash to be a reorganization in *National Pipe & Foundry Company,* 19 B. T. A. 242, and *First National Bank of Champlain, N. Y.,* 21 B. T. A. 415; *Bruce,* 30 B. T. A. 80; *First Seattle Dexter Horton National Bank,* 27 B. T. A. 1242, affirmed 77 Fed. (2d) 45 (C. C. A. 9). Preferred stock was also the pivotal ingredient for reorganization in *Harrison,* 30 B. T. A. 966, and *Fifth Ave. Bank of New York,* 31 B. T. A. 945. It is noteworthy that in the latter case the reorganization conclusion was reached even though the preferred stock was redeemed within 10 days after issuance.

A "recapitalization" has been part of the defini-

tion of reorganization beginning with the Revenue Act of 1921 right through the Revenue Act of 1934 now in force. Article 112(g)-2 of Regulations 86 (promulgated under the 1934 Act) specifically designates a security exchange involving the issuance of preferred stock as constituting a recapitalization, and hence, a reorganization, regardless of the type and features of the preferred stock. See also Article 112(b) (2)-1 of Regulations 86.

Renewing acquaintances with the case at bar, petitioner in the transfer of its assets, acquired in exchange 12,500 shares of preferred stock (constituting the entire authorized and outstanding issue) of the new company. That obviously gave it a continuing interest in the new enterprise. The transaction thus comes squarely within the definition of reorganization implanted in the statute and as interpreted by this Court.

In the face of a conclusion so irresistibly reached, the basis for an opposing position taken by the lower court must necessarily be called up for consideration. Dissecting the opinion below, it will be found that the court believed there were two impediments against the holding of reorganization: first, that petitioner did not acquire a controlling interest over the affairs of the transferee, and second, that petitioner continued in existence. From these, the court concluded that a sale and not a reorganization took place. Petitioner will endeavor to establish that the acquisition of a controlling interest over the transferee is not a prerequisite of reorganization under Part(A) of the statutory definition. Likewise, it will try to show that continued existence of the transferor is not a deterrent; but even if it be, petitioner substantially meets that requirement. If petitioner succeeds in these respects, the foundational structure of the decision below, perforce crashes.

III.

A controlling interest over the transferee corporation is unnecessary for an exchange to qualify as a reorganization under Section 203(h) (1) (A). It is only under Section 203(h) (1) (B) that the element of control becomes a factor.

It may be well at this point to repeat the statutory definition of a reorganization in so far as here material, to see just where and how the element of control of the transferee enters into the picture.

> "(1) The term 'reorganization' means (A) a merger or consolidation (including the acquisition by one corporation of * * * substantially all the properties of another corporation), *or* (B) a transfer by a corporation of all or a part of its assets to another corporation *if immediately after the transfer the transferor or its stockholders or both are in control of the corporation to which the assets are transferred,* * * *."*

The foregoing immediately discloses that it is only the disjunctive part (B) of the definition of reorganization that requires "control". We, here, have nothing to do with (B). If petitioner can find repose anywhere, it is under (A). Now, (A) and (B) are distinct from one another. Their respective provinces are clearly explained in G. C. M. 1753, VI-1 CB 138, as follows:

> "Section 203 (h) (1) (A) is not inconsistent with section 203 (h) (1) (B). One supplements the other. For example, a transfer of all the assets of a corporation constitutes a reorganization under the second part

> of definition (A) irrespective of the element of 80 per cent control demanded by definition (B). Again, a transfer of but a part of the assets of a corporation can never, of itself, result in a reorganization under section 203 (h) (1) (A), but it does result in a reorganization under section 203 (h) (1) (B) if there is present an additional element, namely, immediate control of the transferee corporation by the transferor or its stockholders, or both."

Whether (B) can be engrafted on or fused into (A), as the court below seems to have done, was a field of inquiry that was given most painstaking and comprehensive consideration in *Minnesota Tea Company* v. *Commissioner*, 76 Fed. (2d) 797 (C. C. A. 8), certiorari granted October 14, 1935. After intensively reviewing the wording of the statute, the long-established administrative construction, the avowed intent and purpose of Congress as gleaned from the legislative history of the various Revenue Acts, and the adjudications on the subject, the Eighth Circuit reached the following conclusion:

> "No particular percentage of the stock of the transferee to be received by the transferor is specified or required. We find no ground for holding that the 'continuance of interest' must be of essentially the same interest, or that it must be controlling interest. The provision for percentage of stock to be received, specified in clause (B) reorganizations, has no application here."

The Court is respectfully referred to the full opinion in the quoted case because it is so apposite and illuminating. Some of the other cases, and authorities

to the same effect and not cited in the *Minnesota Tea Company* decision, are collected in the footnote.*

The Tenth Circuit reached an opposite conclusion in *West Texas Refining and Development Company* v. *Commissioner*, 68 Fed. (2d) 77, but it is submitted that its holding in this respect is untenable in view of what has here preceded. Respondent seems to have conceded as much in its petition for a writ of certiorari (page 10) in the *Minnesota Tea Company* case when respondent said "We do not contend, as suggested by the court below, that the requirement of control, found in clause (B), is to be incorporated in clause (A)".

We return to the point of beginning. There is no requirement under (A) that the transferor acquire a controlling interest over the affairs of the transferee. The court below was therefore in error in interposing lack of such interest as defeating petitioner's cause.

IV.

Dissolution of the transferor corporation is unnecessary for an exchange to qualify as a reorganization under Section 203(h) (1) (A); but even if necessary, there has been here substantial compliance with such requirement.

No potency or magic is placed upon dissolution by the statute. In point of fact, dissolution is not

* *Howard* v. *Commissioner*, 56 Fed. (2d) 781 (C. C. A. 6); *Barker*, 28 B. T. A. 657; *Harrison*, *supra*; *Woodward*, 30 B. T. A. 1217; *Armstrong*, 31 B. T. A. 418; *Fifth Ave. National Bank of New York*, *supra*. See also G. C. M. 1345, VI-1 C. B. 15; G. C. M. 747, IX-1 C. B. 184; I. T. 2662, IX-2 C. B. 41. Likewise, Baar and Morris, "Hidden Taxes in Corporate Reorganizations", pp. 47, 85; Satterlee, "The Income Tax Definition of Reorganizations", The Tax Magazine, Vol. XII, p. 639 (Dec. 1934).

even mentioned. If anything, continued existence of the transferor is definitely implied since under the parenthetical matter, the acquisition by one corporation of the majority of the stock of another corporation likewise constitutes a reorganization, and the ownership of the majority of the stock is not ordinarily sufficient to swing a dissolution.

Furthermore, reference to Section 203(c) of the Act brings out forcibly that dissolution may, under given circumstances, destroy rather than create the tax deferred status. Under that section, if a corporation acquires stock in a reorganization and distributes it to its stockholders, the distribution is tax-free to the stockholders provided they do not surrender any of their stock in the distributing corporation, which is another way of saying, providing that the distributing corporation continues in existence. It would be a bizarre rule, indeed, that made dissolution omnipotent under Section 203(h) (1) (A), and at the same time blighted the application of Section 203(c) because of the dissolution.

The lower court evidently had in mind that in a merger, one of the existing corporations is extinguished, and that in a consolidation, all of the existing corporations are extinguished. That is true of literal mergers or consolidations, but we have already seen that the whole idea of the parenthetical clause was to get away from "merger" or "consolidation" in the technical sense, and to expand the field so that even where one corporation does not go out of existence, but instead a majority of its stock or substantially all its properties are acquired by another corporation, in which corporation the transferor acquires a stock interest, the tax consequences are the same as if a strict merger or consolidation took place.

Whether or no dissolution is required under (A) was thoroughly canvassed by the Second Circuit in *John J. Watts* v. *Commissioner,* 75 Fed. (2d) 981, certiorari granted October 14, 1935. The court carefully traced the whole course of the legislative history and administrative construction on the point (to all of which reference is hereby had) to the following end:

> "Having had the opportunity, it is to be presumed that if Congress had intended, contrary to the regulation in force, to have the gain from such an exchange as this be tax free only when there was a dissolution of one of the corporations or some other change in the corporate structure such as would commonly take place in a merger or consolidation, strictly speaking, it would have said so. The fact that it changed a related part of the statute to remove any doubt as to the validity of a regulation and at the same time reenacted the part which had been construed by the regulation which governs here shows an adoption of such construction. *National Lead Co.* v. *United States,* 252 U. S. 140; *United States* v. *Cerecedo Hermanos y Compania,* 209 U. S. 337; *Francisco Sugar Co.* v. *Commissioner,* 47 Fed. (2) 555.

Precisely, the same destination was reached in the *Minnesota Tea Company* case, *supra.* See also *Harrison, supra.* Continued existence of the transferor, therefore, provides no obstacle in the path leading to reorganization.* A different conclusion appears to have been reached by the Fourth Circuit in *The G. and K. Manufacturing Company* v. *Com-*

* See also Baar and Morris, "Hidden Taxes in Corporate Reorganizations", pp. 68, 85; Satterlee, "The Income Tax Definition of Reorganizations", The Tax Magazine, Vol. XII, p. 639 (Dec. 1934).

missioner, 76 Fed. (2d) 454, certiorari granted October 14, 1935. (However, the core of the decision in that case seems to be predicated on the factual question as to whether substantially all of the assets were transferred.)

But even if absence of continued existence of the transferring corporation be assumed a requisite, it would be no thorn in petitioner's path. Petitioner's stockholders voted that the corporation, after consummating the reorganization, "shall cease operation, and the directors and officers thereof shall proceed to liquidate the corporation and cause the same to be dissolved". While a technical dissolution was not effected, the record shows (R. 12) that the corporation has been inactive. Its existence has been nominal in a corporate shell. Its death had been encompassed. All that remained was the burial. That it is the former event that really counts, was set forth in *Aluminum Goods Mfg. Co.* v. *Commissioner,* 56 Fed. (2d) 568 (C. C. A. 6); affirmed 287 U. S. 544. In that case, affiliation rather than reorganization was involved, but the principle is pervasive. Said the court:

> "To ascertain when the status of affiliation terminates, attention is directed to the subsidiary's death, not to its burial."

To the same effect see *Frelmort Realty Corp.,* 29 B. T. A. 181, 186.

The retaining of liabilities to which the court below alludes, has reference to the obligation to pay the 1926 income tax, and the 1926 bonus to employees. These were items requiring prompt liquidation in the ordinary course and tie in with the reservation of $100,000 cash by petitioner. With these items out

of the way, the corporate structure was denuded. The omission to carry out the formality of the dissolution step can not submerge its actuality. The corporate cupboard was bare and its effectual existence terminated.

If, therefore, continued existence must be negatived to comport with reorganization, petitioner may still be counted in the reorganization ranks.

CONCLUSION.

The exchange of substantially all the assets of a corporation for all the preferred stock of the transferee corporation (plus cash) is a reorganization. Neither control of the transferee nor dissolution of the transferor is essential. (The latter, if required, is substantially present in this case.) This conclusion is proclaimed by the statute and ingrained by legislative history, years of administrative interpretation followed by statute reenactment, and judicial opinion.

The decision of the Circuit Court of Appeals should be *reversed*.

Respectfully submitted,

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November, 1935.

APPENDIX.

The Revenue Act of 1926, c. 27, 44 Stat. 9, provides in part as follows:

SEC. 203. (a) Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 202, shall be recognized, except as hereinafter provided in this section.

(b) (2) No gain or loss shall be recognized if stock or securities in a corporation a party to a reorganization are, in pursuance of the plan of reorganization, exchanged solely for stock or securities in such corporation or in another corporation a party to the reorganization.

(3) No gain or loss shall be recognized if a corporation a party to a reorganization exchanges property, in pursuance of the plan of reorganization, solely for stock or securities in another corporation a party to the reorganization.

(c) If there is distributed, in pursuance of a plan of reorganization, to a shareholder in a corporation a party to the reorganization, stock or securities in such corporation or in another corporation a party to the reorganization, without the surrender by such shareholder of stock or securities in such a corporation, no gain to the distributee from the receipt of such stock or securities shall be recognized.

(e) If an exchange would be within the provisions of paragraph (3) of subdivision (b) if it were not for the fact that the property received in exchange consists not only of stock

or securities permitted by such paragraph to be received without the recognition of gain, but also of other property or money, then——

(1) If the corporation receiving such other property or money distributes it in pursuance of the plan of reorganization, no gain to the corporation shall be recognized from the exchange, but

(2) If the corporation receiving such other property or money does not distribute it in pursuance of the plan of reorganization, the gain, if any, to the corporation shall be recognized, but in an amount not in excess of the sum of such money and the fair market value of such other property so received, which is not so distributed.

(h) As used in this section and sections 201 and 204——

(1) The term "reorganization" means (A) a merger or consolidation (including the acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation, or substantially all the properties of another corporation), or (B) a transfer by a corporation of all or a part of its assets to another corporation if immediately after the transfer the transferor or its stockholders or both are in control of the corporation to which the assets are transferred, or (C) a recapitalization, or (D) a mere change in identity, form, or place of organization, however effected.

(2) The term "a party to a reorganization" includes a corporation resulting from a reorganization and includes both corporations

in the case of an acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation.

(i) As used in this section, the term "control" means the ownership of at least 80 per centum of the voting stock and at least 80 per centum of the total number of shares of all other classes of stock of the corporation.

(U. S. C. Sup. V, Title 26, Sec. 934.)